

**REPORT OF THE AUDIT OF THE
KNOTT COUNTY
FISCAL COURT**

**For The Fiscal Year Ended
June 30, 2012**



**ADAM H. EDELEN
AUDITOR OF PUBLIC ACCOUNTS
www.auditor.ky.gov**

**209 ST. CLAIR STREET
FRANKFORT, KY 40601-1817
TELEPHONE (502) 564-5841
FACSIMILE (502) 564-2912**



ADAM H. EDELEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky
Honorable Steven L. Beshear, Governor
Lori H. Flanery, Secretary
Finance and Administration Cabinet
Honorable Randy Thompson, Knott County Judge/Executive
Members of the Knott County Fiscal Court

The enclosed report prepared by Ray, Foley, Hensley & Company, PLLC, Certified Public Accountants, presents the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Knott County, Kentucky, as of and for the year ended June 30, 2012, which collectively comprise the County's basic financial statements.

We engaged Ray, Foley, Hensley & Company, PLLC to perform the audit of these financial statements. We worked closely with the firm during our report review process; Ray, Foley, Hensley & Company, PLLC evaluated Knott County's internal controls and compliance with applicable laws and regulations.

Respectfully submitted,

A handwritten signature in dark ink, appearing to read "Adam H. Edelen".

Adam H. Edelen
Auditor of Public Accounts

Enclosure



EXECUTIVE SUMMARY
AUDIT EXAMINATION OF THE
KNOTT COUNTY FISCAL COURT

June 30, 2012

Ray, Foley, Hensley & Company, PLLC has completed the audit of the Knott County Fiscal Court for fiscal year ended June 30, 2012.

We have issued unqualified opinions on the governmental activities, each major fund, and the aggregate remaining fund information financial statements of Knott County, Kentucky.

In accordance with OMB Circular 133, we have also issued an unqualified opinion on the compliance requirements that are applicable to Knott County Fiscal Court's major federal programs: U.S. Department of Homeland Security - Disaster Grants - Public Assistance (Presidentially Declared Disasters (CFDA # 97.036) and U.S. Department of Agriculture - ARRA Emergency Watershed Protection Program (CFDA #10.923) for the year ended June 30, 2012.

Financial Condition:

The fiscal court had total net assets of \$4,178,232 as of June 30, 2012. The fiscal court had unrestricted net assets of \$1,491,629 in its governmental activities as of June 30, 2012, with total net assets of \$4,178,232. The fiscal court had total debt principal as of June 30, 2012 of \$13,608,071 with \$530,167 due within the next year.

Report Comments:

- 2012-01 The Fiscal Court Should Ensure That All Payments Due Are Made Timely
- 2012-02 The Fiscal Court Should Ensure That Payroll Timesheets Are Signed And Personnel Folders Are Complete
- 2012-03 Knott County Fiscal Court Failed To Fully Restore Restricted Funds

Deposits:

The fiscal court's deposits were insured and collateralized by bank securities or bonds.

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Ray, Foley, Hensley & Company, PLLC

Certified Public Accountants and Consultants

Stephen R. Allen, CPA/PFS
Dennis H. England, CPA
Michael D. Foley, CPA
Lyman Hager, Jr., CPA
Jerry W. Hensley, CPA

J. Carroll Luby, CPA

To the People of Kentucky

Honorable Steven L. Beshear, Governor

Lori H. Flanery, Secretary

Finance and Administration Cabinet

Honorable Randy Thompson, Knott County Judge/Executive

Members of the Knott County Fiscal Court

Independent Auditors' Report

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Knott County, Kentucky, as of and for the year ended June 30, 2012, which collectively comprise the County's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Knott County Fiscal Court. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for Fiscal Court Audits issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As described in Note 1, Knott County, Kentucky, prepares its financial statements in accordance with the modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Knott County, Kentucky, as of June 30, 2012, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with the basis of accounting described in Note 1.

230 Lexington Green Circle, Suite 600 • Lexington, Kentucky 40503-3326

Phone: 859-231-1800 • Fax: 859-422-1800 • Toll-Free: 1-800-342-7299

www.rfhco.com

Members American Institute of Certified Public Accountants and Kentucky Society of Certified Public Accountants

To the People of Kentucky
Honorable Steven L. Beshear, Governor
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Members of the Knott County Fiscal Court

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Knott County, Kentucky's basic financial statements. The combining fund financial statements and budgetary comparison information are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments and Non-Profit Organizations, and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The combining fund financial statements and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining fund financial statements and schedule of expenditures of federal awards are fairly stated in all material respects in relation to the basic financial statements as a whole. The budgetary comparison information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

In accordance with Government Auditing Standards, we have also issued our report dated December 14, 2012 on our consideration of Knott County, Kentucky's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Based on the results of our audit, we present the accompanying schedule of findings and questioned costs included herein, which discusses the following report comments:

- 2012-01 The Fiscal Court Should Ensure That All Payments Due Are Made Timely
- 2012-02 The Fiscal Court Should Ensure That Payroll Timesheets Are Signed And Personnel Folders Are Complete
- 2012-03 Knott County Fiscal Court Failed To Fully Restore Restricted Funds

Ray, Foley, Hensley & Company

Ray, Foley, Hensley & Company, PLLC
December 14, 2012

KNOTT COUNTY OFFICIALS

For The Year Ended June 30, 2012

Fiscal Court Members:

Randy Thompson	County Judge/Executive
Mark Chaffins	Magistrate
Jamie Mosley	Magistrate
Calvin Waddles	Magistrate
Barry Watts	Magistrate

Other Elected Officials:

Timothy Bates	County Attorney
Ricky Prater	Jailer
Kenneth Gayheart	County Clerk
Judy Collins	Circuit Court Clerk
Dale Richardson	Sheriff
Edward Slone	Property Valuation Administrator
Jeff Blair	Coroner

Appointed Personnel:

Kevin Jacobs	County Treasurer
Darrell Madden CPA	Finance Officer

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KNOTT COUNTY
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS

June 30, 2012

KNOTT COUNTY
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS

June 30, 2012

	<u>Governmental Activities</u>
ASSETS	
Current Assets:	
Cash and Cash Equivalents	\$ 1,491,629
Total Current Assets	<u>1,491,629</u>
Noncurrent Assets:	
Capital Assets - Net of Accumulated Depreciation	
Land and Land Improvements	1,054,505
Construction In Progress	
Buildings and Improvements	13,268,092
Vehicles and Equipment	258,610
Infrastructure	<u>1,713,467</u>
Total Noncurrent Assets	<u>16,294,674</u>
Total Assets	<u>17,786,303</u>
LIABILITIES	
Current Liabilities:	
Bonds Payable	503,065
Financing Obligations Payable	<u>27,102</u>
Total Current Liabilities	<u>530,167</u>
Noncurrent Liabilities:	
Bonds Payable	13,019,877
Financing Obligations Payable	<u>58,027</u>
Total Noncurrent Liabilities	<u>13,077,904</u>
Total Liabilities	<u>13,608,071</u>
NET ASSETS	
Invested in Capital Assets, Net of Related Debt	2,686,603
Unrestricted	<u>1,491,629</u>
Total Net Assets	<u><u>\$ 4,178,232</u></u>

The accompanying notes are an integral part of the financial statements.

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KNOTT COUNTY
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS
For The Year Ended June 30, 2012

KNOTT COUNTY
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2012

		Program Revenues Received		
Functions/Programs Reporting Entity	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary Government:				
Governmental Activities:				
General Government	\$ 2,644,916	\$	\$ 362,360	\$
Protection to Persons and Property	1,223,335		87,094	
General Health and Sanitation	3,397,232	120,017	2,220,271	
Social Services	304,209			
Recreation and Culture	2,647,915	360,150	1,814,386	
Roads	2,482,706		3,450,118	2,422,168
Interest on Long-Term Debt	700,241		504,538	
Capital Projects	280,197			
Total Governmental Activities	\$ 13,680,751	\$ 480,167	\$ 8,438,767	\$ 2,422,168

General Revenues:

Taxes:

 Real Property Taxes

 Personal Property Taxes

 Motor Vehicle Taxes

 Other Taxes

Excess Fees

Miscellaneous Revenues

Accrued Interest Received

Total General Revenues and Transfers

Change in Net Assets

Net Assets - Beginning

Net Assets - Ending

The accompanying notes are an integral part of the financial statements.

KNOTT COUNTY
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS
For The Year Ended June 30, 2012
(Continued)

Net (Expenses) Revenues
and Changes in Net Assets
Primary Government

Governmental
Activities

\$	(2,282,556)
	(1,136,241)
	(1,056,944)
	(304,209)
	(473,379)
	3,389,580
	(195,703)
	(280,197)
	<u>(2,339,649)</u>

	310,233
	224,118
	112,500
	864,388
	77,520
	366,884
	10,472
	<u>1,966,115</u>
	(373,534)
	<u>4,551,766</u>
\$	<u><u>4,178,232</u></u>

The accompanying notes are an integral part of the financial statements.

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KNOTT COUNTY
BALANCE SHEET - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

June 30, 2012

KNOTT COUNTY
BALANCE SHEET - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

June 30, 2012

	General Fund	Road Fund	LGEA Fund	State Grants Fund	Debt Service Fund
ASSETS					
Cash and Cash Equivalents	\$ 154,573	\$ 408,328	\$ 39,573	\$ 56,921	\$ 671,994
Due From Other Funds			156,000		
Total Assets	<u>154,573</u>	<u>408,328</u>	<u>195,573</u>	<u>56,921</u>	<u>671,994</u>
LIABILITIES AND FUND BALANCES					
LIABILITIES					
Due To Other Funds	156,000				
Total Liabilities	<u>156,000</u>				
FUND BALANCES					
Committed To:					
Debt Service					671,994
Assigned To:					
Recreation and Culture					
Protection to Persons and Property	2,607				
Roads		408,328			
Unassigned	<u>(4,034)</u>		<u>195,573</u>	<u>56,921</u>	
Total Fund Balances	<u>(1,427)</u>	<u>408,328</u>	<u>195,573</u>	<u>56,921</u>	<u>671,994</u>
Total Liabilities and Fund Balances	<u>\$ 154,573</u>	<u>\$ 408,328</u>	<u>\$ 195,573</u>	<u>\$ 56,921</u>	<u>\$ 671,994</u>

Reconciliation of the Balance Sheet - Governmental Funds to the Statement of Net Assets:

Total Fund Balances	\$ 1,491,629
Amounts Reported For Governmental Activities In The Statement Of Net Assets Are Different Because:	
Capital Assets Used in Governmental Activities Are Not Financial Resources And Therefore Are Not Reported in the Funds.	31,515,146
Accumulated Depreciation	(15,220,472)
Long-term debt is not due and payable in the current period and, therefore, is not reported in the funds.	
Financing Obligations	(85,129)
Bonds	<u>(13,522,942)</u>
Net Assets Of Governmental Activities	<u>\$ 4,178,232</u>

The accompanying notes are an integral part of the financial statements.

KNOTT COUNTY

BALANCE SHEET - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

June 30, 2012

(Continued)

Non- Major Funds	Total Governmental Funds
\$ 160,240	\$ 1,491,629
	156,000
<u>160,240</u>	<u>1,647,629</u>
	<u>156,000</u>
	<u>156,000</u>
	671,994
1,448	1,448
23,945	26,552
	408,328
<u>134,847</u>	<u>383,307</u>
<u>160,240</u>	<u>1,491,629</u>
<u>\$ 160,240</u>	<u>\$ 1,647,629</u>

The accompanying notes are an integral part of the financial statements.

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KNOTT COUNTY
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

For The Year Ended June 30, 2012

KNOTT COUNTY
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

For The Year Ended June 30, 2012

	<u>General Fund</u>	<u>Road Fund</u>	<u>LGFA Fund</u>	<u>State Grants Fund</u>
REVENUES				
Taxes	\$ 1,378,024	\$	\$	\$
Excess Fees	77,520			
Intergovernmental	449,454	1,896,589	3,450,118	4,034,657
Charges for Services	120,017		18,096	
Miscellaneous	253,966	289	78,456	
Interest	1,629	3,347	1,336	2,765
Total Revenues	<u>2,280,610</u>	<u>1,900,225</u>	<u>3,548,006</u>	<u>4,037,422</u>
EXPENDITURES				
General Government	1,225,328		66,580	4,451
Protection to Persons and Property	458,103		196,162	135,374
General Health and Sanitation			166,941	3,230,291
Social Services	2,750		229,454	72,005
Recreation and Culture	1,185		568,410	382,399
Roads		956,088	470,603	
Debt Service:				
Principal	409,365	235,972	3,133	
Interest	77,368	85,937	23	
Bond Issue Costs				
Lawsuit Settlements	2,000			
Capital Projects		25,551	124,651	129,995
Administration	1,216,999	151,190	555,416	
Total Expenditures	<u>3,393,098</u>	<u>1,454,738</u>	<u>2,381,373</u>	<u>3,954,515</u>
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	<u>(1,112,488)</u>	<u>445,487</u>	<u>1,166,633</u>	<u>82,907</u>
Other Financing Sources (Uses)				
Financing Obligation Proceeds	400,000			
Refunding Bond Proceeds				
Refunding Bond Premium				
Payment to Refunded Bond Escrow Agent				
Transfers From Other Funds	1,448,607	823,863	1,399,000	
Transfers To Other Funds	(774,000)	(879,607)	(2,373,663)	(674,151)
Total Other Financing Sources (Uses)	<u>1,074,607</u>	<u>(55,744)</u>	<u>(974,663)</u>	<u>(674,151)</u>
Net Change in Fund Balances	(37,881)	389,743	191,970	(591,244)
Fund Balances - Beginning	36,454	18,585	3,603	648,165
Fund Balances - Ending	<u>\$ (1,427)</u>	<u>\$ 408,328</u>	<u>\$ 195,573</u>	<u>\$ 56,921</u>

The accompanying notes are an integral part of the financial statements.

KNOTT COUNTY
STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
For The Year Ended June 30, 2012
(Continued)

Debt Service Fund	Non- Major Funds	Total Governmental Funds
\$	\$ 133,215	\$ 1,511,239
		77,520
504,538	525,579	10,860,935
	342,054	480,167
	34,173	366,884
70	1,325	10,472
<u>504,608</u>	<u>1,036,346</u>	<u>13,307,217</u>
		1,296,359
	100,244	889,883
		3,397,232
		304,209
	621,813	1,573,807
	512,128	1,938,819
595,000		1,243,470
579,913		743,241
111,517		111,517
		2,000
		280,197
	98,211	2,021,816
<u>1,286,430</u>	<u>1,332,396</u>	<u>13,802,550</u>
<u>(781,822)</u>	<u>(296,050)</u>	<u>(495,333)</u>
		400,000
4,085,000		4,085,000
36,168		36,168
(4,009,651)		(4,009,651)
670,375	444,576	4,786,421
	(85,000)	(4,786,421)
<u>781,892</u>	<u>359,576</u>	<u>511,517</u>
70	63,526	16,184
671,924	96,714	1,475,445
<u>\$ 671,994</u>	<u>\$ 160,240</u>	<u>\$ 1,491,629</u>

The accompanying notes are an integral part of the financial statements.

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**KNOTT COUNTY
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS**

For The Year Ended June 30, 2012

KNOTT COUNTY
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2012

Reconciliation to the Statement of Activities:

Net Change in Fund Balances - Total Governmental Funds	\$	16,184
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Amounts reported for governmental activities in the Statement of Activities are different because Governmental Funds report capital outlays as expenditures. However, in the Statement of Activities the cost of those assets are allocated over their estimated useful lives and reported as depreciation expense.

Capital Outlay		464,416
Depreciation Expense		(1,715,910)
Assets disposed of, net book value		(26,694)

The issuance of long-term debt (e.g. bonds, financing obligations) provides current financial resources to governmental funds, while repayment of principal on long-term debt consumes the current financial resources of Governmental Funds. These transactions, however, have no effect on net assets.

Bond Proceeds		(4,085,000)
Financing Obligations Principal Payments		28,949
Bond Principal Payments		<u>4,944,521</u>

Change in Net Assets of Governmental Activities	\$	<u><u>(373,534)</u></u>
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TO THE FINANCIAL STATEMENTS**

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KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Note 1. Summary of Significant Accounting Policies

A. Basis of Presentation

The county presents its government-wide and fund financial statements in accordance with a modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Under this basis of accounting, assets, liabilities, and related revenues and expenditures are recorded when they result from cash transactions, with a few exceptions. This modified cash basis recognizes revenues when received and expenditures when paid. Notes receivable are recognized on the Statement of Net Assets, but notes receivable are not included and recognized on Balance Sheet - Governmental Funds. Property tax receivables, accounts payable, compensated absences, and donated assets are not reflected in the financial statements.

The State Local Finance Officer does not require the county to report capital assets and infrastructure; however the value of these assets is included in the Statement of Net Assets and the corresponding depreciation expense is included on the Statement of Activities.

B. Reporting Entity

The financial statements of Knott County include the funds, agencies, boards, and entities for which the fiscal court is financially accountable. Financial accountability, as defined by Section 2100 of the Governmental Accounting Standards Board (GASB) Codification of Governmental Accounting and Financial Reporting Standards, as amended by GASB 14 and GASB 39, was determined on the basis of the government's ability to significantly influence operations, select the governing authority, participate in fiscal management and the scope of public service. Consequently, the reporting entity includes organizations that are legally separate from the primary government. Legally separate organizations are reported as component units if either the county is financially accountable or the organization's exclusion would cause the county's financial statements to be misleading or incomplete. Component units may be blended or discretely presented. Blended component units either provide their services exclusively or almost entirely to the primary government, or their governing bodies are substantively the same as the primary government. All other component units are discretely presented.

Blended Component Units

The following legally separate organization provides its services exclusively to the primary government, and the fiscal court is able to impose its will on this organization. This organization's balances and transactions are reported as though they are part of the county's primary government using the blending method.

Knott County, Kentucky Justice Center Corporation - The Justice Center Corporation accounts for the activities of the Justice Center. The Justice Center Corporation issued debt to build facilities and additions of the justice center. The Justice Center Corporation entered into a contract, lease, and option with the County and Administrative Office of The Courts (AOC), Commonwealth of Kentucky. Administrative costs and the related debt are included in the Fiscal Court's financial statements although the Department for Local Government does not require the Fiscal Court to report or budget these funds.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

C. Knott County Elected Officials

Kentucky law provides for election of the officials below from the geographic area constituting Knott County. Pursuant to state statute, these officials perform various services for the Commonwealth of Kentucky, its judicial courts, the fiscal court, various cities and special districts within the county, and the board of education. In exercising these responsibilities, however, they are required to comply with state laws. Audits of their financial statements are issued separately and individually and can be obtained from their respective administrative offices. These financial statements are not required to be included in the financial statements of Knott County, Kentucky.

- Circuit Court Clerk
- County Attorney
- Property Valuation Administrator
- County Clerk
- County Sheriff

D. Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the primary government and its non-fiduciary component units. For the most part, the effect of interfund activities has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on sales, fees, and charges for support. Business-type revenues come mostly from fees charged to external parties for goods or services. Fiduciary funds are not included in these financial statements due to the unavailability of fiduciary funds to aid in the support of government programs.

The statement of net assets presents the reporting entity's non-fiduciary assets and liabilities, the difference between the two being reported as net assets. Net assets are reported in three categories: 1) invested in capital assets, net of related debt - consisting of capital assets, net of accumulated depreciation and reduced by outstanding balances for debt related to the acquisition, construction, or improvement of those assets; 2) restricted net assets - resulting from constraints placed on net assets by creditors, grantors, contributors, and other external parties, including those constraints imposed by law through constitutional provisions or enabling legislation; and 3) unrestricted net assets - those assets that do not meet the definition of restricted net assets or invested in capital assets.

The statement of activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include: 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function; 2) operating grants and contributions; and 3) capital grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Internally dedicated resources such as taxes and unrestricted state funds are reported as general revenues.

Generally and except as otherwise provided by law, property taxes are assessed as of January 1, levied (mailed) November 1, due at discount November 30, due at face value December 31, delinquent January 1 following the assessment, and subject to sale ninety days following April 15.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

D. Government-wide and Fund Financial Statements (Continued)

Funds are characterized as either major or non-major. Major funds are those whose assets, liabilities, revenues, or expenditures/expenses are at least ten percent of the corresponding total (assets, liabilities, etc.) for all funds or type (governmental or proprietary) and whose total assets, liabilities, revenues, or expenditures/expenses are at least five percent of the corresponding total for all governmental and enterprise funds combined. The fiscal court may also designate any fund as major.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds. Major individual governmental funds and major enterprise funds are reported as separate columns in the financial statements.

Governmental Funds

The primary government reports the following major governmental funds:

General Fund - This is the primary operating fund of the fiscal court. It accounts for all financial resources of the general government, except where the Department for Local Government requires a separate fund or where management requires that a separate fund be used for some function. Per the requirements of GASB 54, the county has included the activities of the Jail Fund.

Road Fund - This fund is for road and bridge construction and repair. The primary source of revenue for this fund is state payments for truck license distribution, municipal road aid, and transportation grants. The Department for Local Government requires the fiscal court to maintain these receipts and expenditures separately from the General Fund.

LGEA Fund - The Local Government Economic Assistance fund primarily accounts for funds from Coal Severance and Mineral Severance Taxes. These funds are used to support public service and protection aspects of the government as well as environmental, social services and parks and recreation activities. The Department for Local Government requires the Fiscal Court to maintain these receipts and expenditures separately from the General Fund.

State Grants Fund - The primary purpose of this fund is to account for the grants that are received from various state agencies earmarked for specific projects. The Department for Local Government requires the Fiscal Court to maintain these receipts and expenditures separately from the General Fund.

Debt Service Fund - The purpose of this fund contains the Youth Center general obligation bond issue and the Justice Center Corporation bond issue. Debt service funds are to account for the accumulation of resources for, and the payment of general long-term debt principal and interest.

The primary government also has the following non-major funds: Emergency Management Fund, Forestry Fund, Sports Complex Fund, and Emergency 911 Fund.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

D. Government-wide and Fund Financial Statements (Continued)

Special Revenue Funds:

The Road Fund, Local Government Economic Assistance Fund, State Grants Fund, Forestry Fund, Sports Complex Fund, Emergency Management Fund and the Emergency 911 Fund are presented as special revenue funds. Special revenue funds are to account for the proceeds of specific revenue sources and expenditures that are legally restricted for specific purposes.

Debt Service Fund:

The Debt Service Fund is presented as a debt service fund. Debt service funds are to account for the accumulation of resources for, and the payment of general long-term debt principal and interest.

Proprietary Funds

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary funds principal ongoing operation. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. The principal operating revenues of a county's enterprise funds are charges to customers for sales. Operating expenses for an enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. The Knott County Fiscal Court does not have any proprietary funds at this time.

E. Deposits and Investments

The government's cash and cash equivalents are considered to be cash on hand, demand deposits, certificates of deposit, and short-term investments with original maturities of three months or less from the date of acquisition.

KRS 66.480 authorizes the county to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

F. Capital Assets

Capital assets, which include land, land improvements, buildings, furniture and office equipment, building improvements, machinery, equipment, and infrastructure assets (roads and bridges) that have a useful life of more than one reporting period based on the government's capitalization policy, are reported in the applicable governmental or business-type activities of the government-wide financial statements. Such assets are recorded at historical cost or estimated historical cost when purchased or constructed.

Cost of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's life are not capitalized. Land and Construction In Progress are not depreciated. Interest incurred during construction is not capitalized. Capital assets and infrastructure are depreciated using the straight-line method of depreciation over the estimated useful life of the asset.

	Capitalization Threshold	Useful Life (Years)
Buildings and Building Improvements	\$ 10,000	10-20
Vehicles and Equipment	\$ 10,000	5
Infrastructure	\$ 10,000	5-10

G. Long-term Obligations

In the government-wide financial statements and proprietary fund types in the fund financial statements, long term debt and other long-term obligations are reported as liabilities in the applicable financial statements. The principal amount of bonds, notes and financing obligations are reported.

In the fund financial statements, governmental fund types recognize bond interest, as well as bond issuance costs when received or when paid, during the current period. The principal amount of the debt and interest are reported as expenditures. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures. Debt proceeds are reported as other financing sources.

H. Fund Equity

In the fund financial statements, the difference between the assets and liabilities of governmental funds is reported as fund balance. Fund balance is divided into non-spendable and spendable components, if applicable.

Non-spendable includes amounts that must be maintained intact legally or contractually.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

H. Fund Equity (Continued)

Spendable include the following:

- Restricted-amounts constrained for a specific purpose by external parties, constitutional provisions, or enabling legislation.
- Committed-amounts constrained for a specific purpose by the county using its highest level of decision making authority.
- Assigned-for all governmental funds, other than general fund, any remaining positive amounts not classified as non-spendable, restricted, or committed. For the general fund, amounts constrained by intent to be used for a specified purpose by the County or the delegated county committee or official given authority to assign amounts.
- Unassigned-for the general fund, amounts not classified as non-spendable, restricted, committed or assigned. For all other governmental funds, amount expended in excess of resources that are non-spendable, restricted, committed or assigned.

For resources considered committed, the county issues an ordinance or resolution that can only be changed with another corresponding ordinance or resolution.

For resources considered assigned, the county has designated the County Treasurer to carry out the intent of the fiscal court.

It is the policy of the County to spend restricted resources first, when both restricted and unrestricted resources are available to spend on the activity. Once restricted resources are exhausted, then committed, assigned and unassigned resources will be spent in that order on the activity.

Encumbrances, although not reported on the balance sheet, are purchase orders that will be fulfilled in a subsequent fiscal period. Although the purchase order or contract creates a legal commitment, the fiscal court incurs no liability until performance has occurred on the part of the party with whom the fiscal court has entered into the arrangement. When a government intends to honor outstanding commitments in subsequent periods, such amounts are encumbered. Due to the modified cash basis of accounting, encumbrances can also include invoices for goods or services received at June 30, but not yet paid and not included as an accounts payable. Significant encumbrances at year end are reported by major funds and non-major funds in the aggregate and included with the commitments and contingencies note disclosure, if applicable.

I. Budgetary Information

Annual budgets are adopted on a cash basis of accounting and according to the laws of Kentucky as required by the State Local Finance Officer.

The County Judge/Executive is required to submit estimated receipts and proposed expenditures to the fiscal court by May 1 of each year. The budget is prepared by fund, function, and activity and is required to be adopted by the fiscal court by July 1.

The fiscal court may change the original budget by transferring appropriations at the activity level; however, the fiscal court may not increase the total budget without approval by the State Local Finance Officer. Expenditures may not exceed budgeted appropriations at the activity level.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

J. Related Organizations, Joint Venture, and Jointly Governed Organizations

A related organization is an entity for which a primary government is not financially accountable. It does not impose its will or have a financial benefit or burden relationship, even if the primary government appoints a voting majority of the related organization's governing board. Based on these criteria, the following are considered related organizations the Knott County Fiscal Court: Knott County Health District, Knott County Library District, Knott County Conservation District, and the Knott County Water District.

A legal entity or other organization that results from a contractual agreement and that is owned, operated, or governed by two or more participants as a separate activity subject to joint control, in which the participants retain (a) an ongoing financial interest or (b) an ongoing financial responsibility is a joint venture. Based upon these criteria, the Knott County Fiscal Court is not involved in any known joint ventures.

Note 2. Deposits

The primary government maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) as required by KRS 66.480(1)(d). According to KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the county and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. These requirements were met.

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the government's deposits may not be returned. The government does not have a deposit policy for custodial credit risk, but rather follows the requirements of KRS 41.240 (4). As of June 30, 2012, all deposits were covered by FDIC insurance or a properly executed collateral security agreement.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 3. Interfund Transfers

	General Fund	Road Fund	LGEA Fund	State Grants Fund	Debt Service Fund	Non-Major Governmental Funds	Total Transfers In
General Fund	\$	\$ 179,607	\$ 1,214,000	\$	\$	\$ 55,000	\$ 1,448,607
Road Fund			823,863				823,863
LGEA Fund	669,000	700,000				30,000	1,399,000
State Grants Fund				670,375			670,375
Debt Service Fund				3,776			444,576
Non-Major	105,000		335,800				
Total Transfers Out	<u>\$ 774,000</u>	<u>\$ 879,607</u>	<u>\$ 2,373,663</u>	<u>\$ 674,151</u>	<u>\$</u>	<u>\$ 85,000</u>	<u>\$ 4,786,421</u>

Note 4. Capital Assets

Capital asset activity for the year ended June 30, 2012, was as follows:

	Reporting Entity		
	Beginning Balance	Increases	Ending Balance
<u>Governmental Activities:</u>			
Capital Assets Not Being Depreciated:			
Land and Land Improvements	\$ 1,054,505	\$	\$ 1,054,505
Construction In Progress	44,500		44,500
Total Capital Assets Not Being Depreciated	<u>1,099,005</u>		<u>1,054,505</u>
Capital Assets, Being Depreciated:			
Buildings	20,468,599	267,961	20,736,560
Vehicles and Equipment	1,918,257		1,696,405
Infrastructure	7,786,721	240,955	8,027,676
Total Capital Assets Being Depreciated	<u>30,173,577</u>	<u>508,916</u>	<u>30,460,641</u>
Less Accumulated Depreciation For:			
Buildings	(6,455,014)	(1,013,454)	(7,468,468)
Vehicles and Equipment	(1,559,021)	(73,931)	(1,437,795)
Infrastructure	(5,685,684)	(628,525)	(6,314,209)
Total Accumulated Depreciation	<u>(13,699,719)</u>	<u>(1,715,910)</u>	<u>(15,220,472)</u>
Total Capital Assets, Being Depreciated, Net	<u>16,473,858</u>	<u>(1,206,994)</u>	<u>15,240,169</u>
Governmental Activities Capital Assets, Net	<u>\$ 17,572,863</u>	<u>\$ (1,206,994)</u>	<u>\$ 16,294,674</u>

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 4. Capital Assets (Continued)

Depreciation expense was charged to functions of the primary government as follows:

<u>Governmental Activities:</u>	
General Government	\$ 104,864
Protection to Persons and Property	315,797
Recreation and Culture	661,597
Roads, Including Depreciation of General Infrastructure Assets	<u>633,652</u>
Total Depreciation Expense - Governmental Activities	<u>\$ 1,715,910</u>

Note 5. Short-term Debt

During the year ended June 30, 2012, the County entered into a loan in the amount of \$400,000 from Community Trust Bank, bearing interest at a rate of 3.5%. The note had a maturity date of June 29, 2012. The County paid this loan off on April 26, 2012, and therefore had no balance at June 30, 2012.

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Primary Government:				
<u>Governmental Activities:</u>				
Financing Obligations	\$	\$ 400,000	\$ 400,000	\$
Governmental Activities				
Short-term Liabilities	<u>\$ 0</u>	<u>\$ 400,000</u>	<u>\$ 400,000</u>	<u>\$ 0</u>

Note 6. Long-term Debt

A. General Obligation Road Bonds, Series 2007

The Fiscal Court issued \$1,500,000 in obligations during 2007. The bonds are payable in semi-annual installments, principal and interest, beginning January 1, 2008, in the amount of \$98,522. Interest accrues at the rate of 5.5%. The Fiscal Court issued the bonds for various road projects. As of June 30, 2012, bonds outstanding were \$852,942. Future principal and interest requirements are:

<u>Fiscal Year Ended June 30</u>	<u>Governmental Activities</u>	
	<u>Scheduled Interest</u>	<u>Scheduled Principal</u>
2013	\$ 23,409	\$ 75,113
2014	40,564	156,480
2015	31,840	165,205
2016	22,629	174,416
2017	12,904	184,141
2018	<u>2,637</u>	<u>95,885</u>
Totals	<u>\$ 133,983</u>	<u>\$ 851,240</u>

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 6. Long-term Debt (Continued)

B. Kentucky River Regional Jail Bond, Series 2007

The Perry County Fiscal Court issued \$4,975,000 of general obligation refunding bonds to build the Kentucky River Regional Jail. The Knott County Fiscal Court began using this facility as its jail upon completion. To use the facility, the Knott County Fiscal Court is required to pay twenty-five percent (25%) of the amount of each principal and interest payment. Principal payments are due annually starting on December 1, 2008. Interest is payable semi-annually starting June 1, 2008. The Knott County Fiscal Court was initially responsible for \$1,243,750 in principal payments on the bonds. The interest is calculated at a rate of 3.85%. As of June 30, 2012, the bonds outstanding were \$1,225,000. Future principal and interest requirements are:

Fiscal Year Ended June 30	Governmental Activities	
	Scheduled Interest	Scheduled Principal
2013	\$ 67,423	\$ 116,250
2014	41,532	60,000
2015	39,174	62,500
2016	36,695	66,250
2017	34,097	68,750
2018-2022	127,916	385,000
2023-2027	46,176	466,250
Totals	<u>\$ 393,013</u>	<u>\$ 1,225,000</u>

C. General Obligation Bonds, Series 2002 S/F

The Knott County Justice Center Corporation issued \$6,605,000 in obligations during 2002. The bonds are payable in annual installments with the interest payable in semi-annual installments, beginning October 1, 2002. Interest accrues at a rate of 4.78%. The Justice Center Corporation issued the bonds to fund the building of the Justice Center. As of June 30, 2012, bonds outstanding were \$4,130,000. This amount was in escrow due to its refunding in October 2012 (see note D). This amount is included in the debt reduction amount in note I.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 6. Long-term Debt (Continued)

D. General Obligation Bonds, Series 2002 S/F

The Knott County, Kentucky Justice Center Corporation issued \$4,085,000 First Mortgage Refunding Revenue bonds dated October 19, 2011. The bonds are payable in annual installments with the interest payable in semi-annual installments, beginning April 1, 2012. Interest accrues at rates of 1.0% to 3.25%. The Justice Center Corporation issued the bonds to refund the General Obligation bonds, Series 2002 S/F (see note C). As of June 30, 2012, bonds outstanding were \$4,085,000. This transaction created an economic gain of \$210,765 while saving the County \$482,802 in principal and interest payments. Future principal and interest requirements are:

Fiscal Year Ended June 30	Governmental Activities	
	Scheduled Interest	Scheduled Principal
2013	\$ 96,450	\$
2014	94,900	310,000
2015	89,500	385,000
2016	81,700	395,000
2017	73,750	400,000
2018-2022	227,707	2,130,000
2023	7,556	465,000
Totals	<u>\$ 671,563</u>	<u>\$ 4,085,000</u>

E. General Obligation Improvement Bonds, Series 2006 S/F

The Fiscal Court issued \$8,450,000 in obligations during 2006. The bonds are payable in annual installments with the interest payable in semi-annual installments, beginning March 1, 2007. Interest accrues at a rate of 5.00%. The Fiscal Court issued the bonds to fund the building of the Youth and Recreation Center. As of June 30, 2012, bonds outstanding were \$7,360,000. Future principal and interest requirements are:

Fiscal Year Ended June 30	Governmental Activities	
	Scheduled Interest	Scheduled Principal
2013	\$ 360,250	\$ 310,000
2014	344,375	325,000
2015	327,750	340,000
2016	310,250	360,000
2017	291,875	375,000
2018-2022	1,150,090	2,190,000
2023-2027	528,000	2,810,000
2028	16,250	650,000
Totals	<u>\$ 3,328,840</u>	<u>\$ 7,360,000</u>

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 6. Long-term Debt (Continued)

F. Other Obligation

The Fiscal Court has an outstanding obligation to Fern Taylor. Ms. Taylor's husband died while on the job as a Deputy Sheriff. At the time, the Fiscal Court agreed to pay Ms. Taylor \$122 bi-weekly until her death. Future principal requirements are:

Fiscal Year Ended June 30	Governmental Activities	
	Scheduled Interest	Scheduled Principal
2013	\$	\$ 3,172
2014		3,172
2015		3,172
2016		3,172
2017		3,172
2018		3,172
Totals	\$ 0	\$ 19,032

G. Grader

The Fiscal Court has a lease with Hyden Citizens Bank for a grader. Monthly payments are required in the amount of \$2,195 including interest. The lease matures on February 10, 2015. Future principal and interest requirements are:

Fiscal Year Ended June 30	Governmental Activities	
	Scheduled Interest	Scheduled Principal
2013	\$ 2,564	\$ 23,930
2014	1,434	24,908
2015	302	17,259
Totals	\$ 4,300	\$ 66,097

H. Loader

The Fiscal Court had a lease with Farmers Bank for a loader. Monthly payments were required in the amount of \$1,035 including interest. In October 2011, the Fiscal Court paid the lease off.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 6. Long-term Debt (Continued)

I. Changes In Long-term Liabilities

Long-term liability activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Primary Government:					
<u>Governmental Activities:</u>					
General Obligation Bonds	\$ 14,382,463	\$	\$ 4,944,521	\$ 9,437,942	\$ 503,065
Revenue Bonds		4,085,000		4,085,000	
Financing Obligations	114,078		28,949	85,129	27,102
Governmental Activities					
Long-term Liabilities	<u>\$ 14,496,541</u>	<u>\$ 4,085,000</u>	<u>\$ 4,973,470</u>	<u>\$13,608,071</u>	<u>\$ 530,167</u>

Note 7. Employee Retirement System

The fiscal court has elected to participate in the County Employees Retirement System (CERS), pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a cost sharing, multiple employer defined benefit pension plan, which covers all eligible full-time employees and provides for retirement, disability and death benefits to plan members. Benefit contributions and provisions are established by statute.

Nonhazardous covered employees are required to contribute 5 percent of their salary to the plan. Nonhazardous covered employees who begin participation on or after September 1, 2008 are required to contribute 6 percent of their salary to the plan. The county's contribution rate for nonhazardous employees was 18.96 percent.

Hazardous covered employees are required to contribute 8 percent of their salary to the plan. Hazardous covered employees who begin participation on or after September 1, 2008 are required to contribute 9 percent of their salary to be allocated as follows: 8% will go to the member's account and 1% will go to the KRS insurance fund. The county's contribution rate for hazardous employees was 35.76 percent.

The county's contribution for FY 2010 was \$350,484, FY 2011 was \$386,453, and FY 2012 was \$417,458.

Benefits fully vest on reaching five years of service for nonhazardous employees. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65. Nonhazardous employees who begin participation on or after September 1, 2008 must meet the rule of 87 (members age plus years of service credit must equal 87, and the member must be a minimum of 57 years of age) or the member is age 65, with a minimum of 60 months service credit.

Aspects of benefits for hazardous employees include retirement after 20 years of service or age 55. For hazardous employees who begin participation on or after September 1, 2008 aspects of benefits include retirement after 25 years of service or the member is age 60, with a minimum of 60 months of service credit.

Note 7. Employee Retirement System (Continued)

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

CERS also provides post retirement health care coverage as follows:

For members participating prior to July 1, 2003, years of service and respective percentages of the maximum contribution are as follows:

Years of Service	% paid by Insurance Fund	% Paid by Member through Payroll Deduction
20 or more	100%	0%
15-19	75%	25%
10-14	50%	50%
4-9	25%	75%
Less than 4	0%	100%

As a result of House Bill 290 (2004 General Assembly), medical insurance benefits are calculated differently for members who began participation on or after July 1, 2003. Once members reach a minimum vesting period of ten years, non-hazardous employees whose participation began on or after July 1, 2003, earn ten dollars per month for insurance benefits at retirement for every year of earned service without regard to a maximum dollar amount.

Hazardous employees whose participation began on or after July 1, 2003, earn fifteen dollars per month for insurance benefits at retirement for every year of earned service without regard to a maximum dollar amount. Upon the death of a hazardous employee, such employee's spouse receives ten dollars per month for insurance benefits for each year of the deceased employee's hazardous service. This dollar amount is subject to adjustment annually based on the retiree cost of living adjustment, which is updated annually due to changes in the Consumer Price Index.

Historical trend information showing the CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report. This report may be obtained by writing the Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, KY 40601-6124, or by telephone at (502) 564-4646.

Note 8. Deferred Compensation

The Knott County Fiscal Court voted to allow all eligible employees to participate in deferred compensation plans administered by The Kentucky Public Employees' Deferred Compensation Authority. The Kentucky Public Employees' Deferred Compensation Authority is authorized under KRS 18A.230 to 18A.275 to provide administration of tax sheltered supplemental retirement plans for all state, public school and university employees and employees of local political subdivisions that have elected to participate.

These deferred compensation plans permits all full time employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. Participation by eligible employees in the deferred compensation plans is voluntary.

Historical trend information showing The Kentucky Public Employees' Deferred Compensation Authority's progress in accumulating sufficient assets to pay benefits when due is presented in The Kentucky Public Employees' Deferred Compensation Authority's annual financial report. This report may be obtained by writing Kentucky Public Employees' Deferred Compensation Authority at 101 Sea Hero Road, Suite 110, Frankfort, KY 40601-8862, or by telephone at (502) 573-7925.

KNOTT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

Note 9. Insurance

For the fiscal year ended June 30, 2012, Knott County was a member of the Kentucky Association of Counties' All Lines Fund (KALF). KALF is a self-insurance fund and was organized to obtain lower cost coverage for general liability, property damage, public officials' errors and omissions, public liability, and other damages. The basic nature of a self-insurance program is that of a collectively shared risk by its members. If losses incurred for covered claims exceed the resources contributed by the members, the members are responsible for payment of the excess losses.

Note 10. Related Party Transactions

Judge Thompson is the president of The Knott County Youth Foundation. The Foundation leases the land on which the sports complex resides. The Fiscal Court in turn, is leasing the land from the Foundation for an amount of \$0 per year. Additionally, the Fiscal Court entered into a second lease for more land adjacent to the sports complex during the year ended December 31, 2010. This lease calls for payments of \$100 per year for the 100 year term.

The Fiscal Court uses a sign company from time to time to manufacture advertising signs in the Sportsplex, the Knott County "Trail Ride" and other miscellaneous items. This sign company is owned by the Judge's sister. The Fiscal Court paid this company \$360 for signs during the year ended June 30, 2012.

The Sportsplex employs several of the Judge's family members on a part-time seasonal basis. Individual payments for wages were \$5,257.

Note 11. Subsequent Events

The County has evaluated and considered the need to recognize or disclose subsequent events through December 14, 2012 which represents the date that these financial statements were available to be issued. Subsequent events past this date, as they pertain to the fiscal year ended June 30, 2012, have not been evaluated by the County.

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**KNOTT COUNTY
COMBINING BALANCE SHEET -
NON-MAJOR GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
Supplementary Information**

June 30, 2012

KNOTT COUNTY
COMBINING BALANCE SHEET -
NON-MAJOR GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
Supplementary Information

June 30, 2012

	Emergency Management Fund	Forestry Fund	Sports Complex Fund	E-911 Fund	Total Non-Major Governmental Funds
ASSETS					
Cash and Cash Equivalents	\$ 65,755	\$ 23,945	\$ 1,448	\$ 69,092	\$ 160,240
Total Assets	<u>65,755</u>	<u>23,945</u>	<u>1,448</u>	<u>69,092</u>	<u>160,240</u>
FUND BALANCES					
Assigned:					
Recreation and Culture			1,448		1,448
Protection to Persons and Property		23,945			23,945
Unassigned	<u>65,755</u>			<u>69,092</u>	<u>134,847</u>
Total Fund Balances	<u>\$ 65,755</u>	<u>\$ 23,945</u>	<u>\$ 1,448</u>	<u>\$ 69,092</u>	<u>\$ 160,240</u>

The accompanying notes are an integral part of the financial statements.

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KNOTT COUNTY
COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - NON-MAJOR GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
Supplementary Information

For The Year Ended June 30, 2012

KNOTT COUNTY
COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - NON-MAJOR GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
Supplementary Information

For The Year Ended June 30, 2012

	Emergency Management Fund	Forestry Fund	Sports Complex Fund	E-911 Fund	Total Non-Major Governmental Funds
REVENUES					
Taxes	\$	\$ 18,423	\$	\$ 114,792	\$ 133,215
Intergovernmental	525,579				525,579
Charges for Services			342,054		342,054
Miscellaneous			34,173		34,173
Interest	461	71	236	557	1,325
Total Revenues	<u>526,040</u>	<u>18,494</u>	<u>376,463</u>	<u>115,349</u>	<u>1,036,346</u>
EXPENDITURES					
Protection to Persons and Property		2,118		98,126	100,244
Recreation and Culture			621,813		621,813
Roads	512,128				512,128
Administration			80,556	17,655	98,211
Total Expenditures	<u>512,128</u>	<u>2,118</u>	<u>702,369</u>	<u>115,781</u>	<u>1,332,396</u>
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	<u>13,912</u>	<u>16,376</u>	<u>(325,906)</u>	<u>(432)</u>	<u>(296,050)</u>
Other Financing Sources (Uses)					
Transfers From Other Funds	124,000		320,576		444,576
Transfers To Other Funds	<u>(85,000)</u>				<u>(85,000)</u>
Total Other Financing Sources (Uses)	<u>39,000</u>		<u>320,576</u>		<u>359,576</u>
Net Change in Fund Balances	52,912	16,376	(5,330)	(432)	63,526
Fund Balances - Beginning	<u>12,843</u>	<u>7,569</u>	<u>6,778</u>	<u>69,524</u>	<u>96,714</u>
Fund Balances - Ending	<u>\$ 65,755</u>	<u>\$ 23,945</u>	<u>\$ 1,448</u>	<u>\$ 69,092</u>	<u>\$ 160,240</u>

The accompanying notes are an integral part of the financial statements.

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KNOTT COUNTY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

KNOTT COUNTY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Fiscal Year Ended June 30, 2012

Federal Grantor		
Program Title	Pass-Through	
<u>Grant Name (CFDA #)</u>	<u>Grantor's Number</u>	<u>Expenditures</u>
<u>U.S Department of Agriculture</u>		
Direct Award		
ARRA-Emergency Watershed Protection Program		
(CFDA # 10.923)	68-5C16-11-079	\$ 22,500
	68-5C16-11-097	25,290
	68-5C16-11-105	95,400
	68-5C16-11-126	15,300
	68-5C16-11-152	36,772
	68-5C16-12-029	132,450
		*** 327,712
Direct Award		
Community Facilities Loans and Grants		
(CFDA # 10.766)		
Sheriff's Vehicles Grant	N/A	1,731
Water Vehicles and Equipment Grant	N/A	109,369
		111,100
Total U.S. Department of Agriculture		438,812
<u>U.S. Department of Health and Human Services</u>		
Passed Through State Cabinet for Health and Family Services		
Department for Aging and Independent Living		
Passed Through Kentucky River Area Development District		
Title III B (CFDA # 93.044)	N/A	22,729
Title III C1 (CFDA # 93.045)	N/A	35,106
Title III C2 (CFDA # 93.045)	N/A	22,779
Nutritional Services Incentive Program (CFDA # 93.053)	N/A	4,730
Cluster Total		85,344
Title III D (CFDA # 93.043)	N/A	1,671
Total U.S. Department of Health and Human Services		87,015
<u>U.S. Department of Homeland Security</u>		
Passed Through State Department Of Military Affairs:		
(CFDA # 97.036)		
Disaster Grants - Public Assistance		
(Presidentially Declared Disasters)	FEMA 1976 DR KY	205,468
Disaster Grants - Public Assistance		
(Presidentially Declared Disasters)	FEMA 4008 DR KY	188,572
		*** 394,040
(CFDA # 97.036)		
Emergency Management Assistance Program	PON2 1100000669 1	5,624
Emergency Management Assistance Program	PON2 1200000383 1	5,345
		10,969
Total U.S. Department of Homeland Security		405,009
Total Expenditures of Federal Awards		\$ 930,836
*** Tested as Major Programs		

KNOTT COUNTY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Fiscal Year Ended June 30, 2012

Note 1 - The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of Knott County, Kentucky and is presented on a modified cash basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations.

KNOTT COUNTY
BUDGETARY COMPARISON INFORMATION
Other Information - Modified Cash Basis

For The Year Ended June 30, 2012

KNOTT COUNTY
BUDGETARY COMPARISON INFORMATION
Other Information - Modified Cash Basis
For The Year Ended June 30, 2012

GENERAL FUND				
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes	\$ 1,291,800	\$ 1,407,650	\$ 1,378,024	\$ (29,626)
In Lieu Tax Payments	5,000	5,000		(5,000)
Excess Fees		77,500	77,520	20
Intergovernmental Revenue	423,330	466,380	362,360	(104,020)
Charges for Services	120,000	120,000	120,017	17
Miscellaneous	121,000	247,600	249,261	1,661
Interest	1,000	1,275	1,262	(13)
Total Revenues	<u>1,962,130</u>	<u>2,325,405</u>	<u>2,188,444</u>	<u>(136,961)</u>
EXPENDITURES				
General Government	1,127,067	1,317,667	1,225,328	92,339
Protection to Persons and Property	2,300	4,800	4,543	257
Social Services	6,000	6,000	2,750	3,250
Recreation and Culture		1,200	1,185	15
Debt Service	3,172	413,172	412,702	470
Administration	1,103,198	1,184,194	1,097,873	86,321
Total Expenditures	<u>2,241,737</u>	<u>2,927,033</u>	<u>2,744,381</u>	<u>182,652</u>
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	<u>(279,607)</u>	<u>(601,628)</u>	<u>(555,937)</u>	<u>45,691</u>
OTHER FINANCING SOURCES (USES)				
Financing Obligation Proceeds		400,000	400,000	
Transfers From Other Funds	179,607	179,607	903,607	724,000
Transfers To Other Funds			(774,000)	(774,000)
Total Other Financing Sources (Uses)	<u>179,607</u>	<u>579,607</u>	<u>529,607</u>	<u>(50,000)</u>
Net Changes in Fund Balance	(100,000)	(22,021)	(26,330)	(4,309)
Fund Balance - Beginning	<u>100,000</u>	<u>22,021</u>	<u>22,007</u>	<u>(14)</u>
Fund Balance - Ending	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ (4,323)</u>	<u>\$ (4,323)</u>

KNOTT COUNTY
BUDGETARY COMPARISON INFORMATION
Other Information - Modified Cash Basis
For The Year Ended June 30, 2012
(Continued)

	ROAD FUND			
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Intergovernmental Revenue	\$ 1,196,296	\$ 1,899,546	\$ 1,896,589	\$ (2,957)
Miscellaneous	1,000	1,000	289	(711)
Interest	3,000	3,000	3,347	347
Total Revenues	1,200,296	1,903,546	1,900,225	(3,321)
EXPENDITURES				
Roads	519,500	967,738	956,088	11,650
Debt Service	225,000	324,100	321,909	2,191
Capital Projects		26,000	25,551	449
Administration	326,189	424,686	151,190	273,496
Total Expenditures	1,070,689	1,742,524	1,454,738	287,786
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	129,607	161,022	445,487	284,465
OTHER FINANCING SOURCES (USES)				
Transfers From Other Funds			823,863	823,863
Transfers To Other Funds	(179,607)	(179,607)	(879,607)	(700,000)
Total Other Financing Sources (Uses)	(179,607)	(179,607)	(55,744)	123,863
Net Changes in Fund Balance	(50,000)	(18,585)	389,743	408,328
Fund Balance - Beginning	50,000	18,585	18,585	
Fund Balance - Ending	\$ 0	\$ 0	\$ 408,328	\$ 408,328

KNOTT COUNTY
BUDGETARY COMPARISON INFORMATION
Other Information - Modified Cash Basis
For The Year Ended June 30, 2012
(Continued)

LOCAL GOVERNMENT ECONOMIC ASSISTANCE FUND

	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Intergovernmental Revenue	\$ 3,800,000	\$ 3,800,000	\$ 3,450,118	\$ (349,882)
Charges for Services	80,000	82,200	18,096	(64,104)
Miscellaneous	11,000	78,700	78,456	(244)
Interest	1,000	1,000	1,336	336
Total Revenues	3,892,000	3,961,900	3,548,006	(413,894)
EXPENDITURES				
General Government	47,500	69,160	66,580	2,580
Protection to Persons and Property	251,002	234,819	196,162	38,657
General Health and Sanitation	149,801	178,041	166,941	11,100
Social Services	304,000	273,385	229,454	43,931
Recreation and Culture	834,600	815,484	568,410	247,074
Roads	672,000	672,000	470,603	201,397
Debt Service	3,200	3,200	3,156	44
Capital Projects	40,000	125,000	124,651	349
Administration	664,897	619,414	555,416	63,998
Total Expenditures	2,967,000	2,990,503	2,381,373	609,130
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	925,000	971,397	1,166,633	195,236
OTHER FINANCING SOURCES (USES)				
Transfers From Other Funds			1,399,000	1,399,000
Transfers To Other Funds	(975,000)	(975,000)	(2,373,663)	(1,398,663)
Total Other Financing Sources (Uses)	(975,000)	(975,000)	(974,663)	337
Net Changes in Fund Balances	(50,000)	(3,603)	191,970	195,573
Fund Balances - Beginning	50,000	3,603	3,603	
Fund Balances - Ending	\$ 0	\$ 0	\$ 195,573	\$ 195,573

KNOTT COUNTY
BUDGETARY COMPARISON INFORMATION
Other Information - Modified Cash Basis
For The Year Ended June 30, 2012
(Continued)

	STATE GRANTS FUND			
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Intergovernmental Revenue	\$ 4,000,000	\$ 5,153,023	\$ 4,034,657	\$ (1,118,366)
Interest	3,000	3,000	2,765	(235)
Total Revenues	4,003,000	5,156,023	4,037,422	(1,118,601)
EXPENDITURES				
General Government		4,600	4,451	149
Protection to Persons and Property	150,000	169,500	135,374	34,126
General Health and Sanitation	1,100,000	3,231,700	3,230,291	1,409
Social Services	25,000	72,550	72,005	545
Recreation and Culture	500,000	382,704	382,399	305
Capital Projects	1,100,000	129,995	129,995	
Administration	528,000	1,113,139		1,113,139
Total Expenditures	3,403,000	5,104,188	3,954,515	1,149,673
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	600,000	51,835	82,907	31,072
OTHER FINANCING SOURCES (USES)				
Transfers From Other Funds				
Transfers To Other Funds	(700,000)	(700,000)	(674,151)	25,849
Total Other Financing Sources (Uses)	(700,000)	(700,000)	(674,151)	25,849
Net Changes in Fund Balances	(100,000)	(648,165)	(591,244)	56,921
Fund Balances - Beginning	100,000	648,165	648,165	
Fund Balances - Ending	\$ 0	\$ 0	\$ 56,921	\$ 56,921

KNOTT COUNTY
NOTES TO OTHER INFORMATION

June 30, 2012

Budgetary Information

Annual budgets are adopted on a cash basis of accounting and according to the laws of Kentucky as required by the State Local Finance Officer.

The County Judge/Executive is required to submit estimated receipts and proposed expenditures to the fiscal court by May 1 of each year. The budget is prepared by fund, function, and activity and is required to be adopted by the fiscal court by July 1.

The fiscal court may change the original budget by transferring appropriations at the activity level; however, the fiscal court may not increase the total budget without approval by the State Local Finance Officer. Expenditures may not exceed budgeted appropriations at the activity level.

Reconciliation to the Statement of Revenue, Expenditures and Fund Balances

General Fund:

**Reconciliation to the Statement of Revenue, Expenditures
And Changes In Fund Balances**

Total Revenues Per Budgetary Information	\$ 2,188,444
Add: Jail Fund Revenues	92,165
Add: Federal Grant Fund Revenues	<u>1</u>
Total Revenue to Statement	<u>\$ 2,280,610</u>
 Total Expenditures Per Budgetary Information	 \$ 2,744,381
Add: Jail Fund Expenditures	648,717
Add: Federal Grant Fund Expenditures	<u>0</u>
Total Expenditures to Statement	<u>\$ 3,393,098</u>
 Other Financing Sources Per Budgetary Information	 \$ 529,607
Add: Transfers to Jail Fund From LGEA Fund	<u>545,000</u>
Total Other Financing Sources (Uses) to Statement	<u>\$ 1,074,607</u>
 Fund Balance-Prior Year Per Budgetary Information	 \$ 22,007
Add: Jail Fund Prior Year Balance	14,159
Add: Federal Grant Fund Prior Year Balance (From Non-Major Funds)	<u>288</u>
General Fund Beginning Balance to Statement	<u>36,454</u>
 Fund Balance-Ending Per Budgetary Information	 (4,323)
Add: Jail Fund Balance-Ending	2,607
Add: Federal Grant Fund Balance-Ending	<u>289</u>
Total Fund Balance-Ending to Statement	<u>\$ (1,427)</u>

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND
ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

The Honorable Randy Thompson, Knott County Judge/Executive
Members of the Knott County Fiscal Court

**Report On Internal Control Over Financial Reporting And
On Compliance And Other Matters Based On An Audit Of Financial
Statements Performed In Accordance With Government Auditing Standards**

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Knott County, Kentucky, as of and for the year ended June 30, 2012, which collectively comprise the County's basic financial statements, as listed in the table of contents and have issued our report thereon dated December 14, 2012. Knott County presents its financial statements on the modified cash basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the Knott County Fiscal Court is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Knott County Fiscal Court's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Knott County Fiscal Court's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Knott County Fiscal Court's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified a certain deficiency in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs as item 2012-02 that we consider to be a significant deficiency in internal control over financial reporting. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Report On Internal Control Over Financial Reporting
And On Compliance And Other Matters Based On An Audit Of Financial
Statements Performed In Accordance With Government Auditing Standards
(Continued)

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Knott County's financial statements as of and for the year ended June 30, 2012, are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items 2012-01, 2012-02, and 2012-03.

The Knott County Judge/Executive's responses to the findings identified in our audit are included in the schedule of findings and questioned costs. We did not audit the County Judge/Executive's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management, others within the entity, the Department for Local Government, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ray, Foley, Hensley & Company

Ray, Foley, Hensley & Company, PLLC
December 14, 2012

**REPORT ON COMPLIANCE WITH REQUIREMENTS
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**



Ray, Foley, Hensley & Company, PLLC

Certified Public Accountants and Consultants

Stephen R. Allen, CPA/PFS
Dennis H. England, CPA
Michael D. Foley, CPA
Lyman Hager, Jr., CPA
Jerry W. Hensley, CPA

J. Carroll Luby, CPA

The Honorable Randy Thompson, Knott County Judge/Executive
Members of the Knott County Fiscal Court

Report On Compliance With Requirements
That Could Have A Direct And Material Effect On Each Major Program
And On Internal Control Over Compliance In Accordance With OMB Circular A-133

Independent Auditor's Report

Compliance

We have audited the compliance of Knott County, Kentucky, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012. Knott County's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Knott County's management. Our responsibility is to express an opinion on Knott County's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Knott County's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Knott County's compliance with those requirements.

In our opinion, Knott County complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

Internal Control Over Compliance

The management of Knott County is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Knott County's internal control over compliance with requirements that could have a direct and material effect on a major federal program as a basis for designing our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Knott County's internal control over compliance.

230 Lexington Green Circle, Suite 600 • Lexington, Kentucky 40503-3326

Phone: 859-231-1800 • Fax: 859-422-1800 • Toll-Free: 1-800-342-7299

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Report On Compliance With Requirements
That Could Have A Direct And Material Effect On Each Major Program
And On Internal Control Over Compliance In Accordance With OMB Circular A-133
(Continued)

Internal Control Over Compliance (Continued)

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, others within the entity, the Department for Local Government, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ray, Foley, Hensley & Company

Ray, Foley, Hensley & Company, PLLC
December 14, 2012

KNOTT COUNTY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

For The Year Ended June 30, 2012

**KNOTT COUNTY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS**

Fiscal Year Ended June 30, 2012

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses unqualified opinions on the governmental activities, each major fund, and the aggregate remaining fund information of Knott County.
2. One significant deficiency relating to the audit of the financial statements is reported in the Independent Auditor's Report.
3. Three instances of noncompliance material to the financial statements of Knott County were disclosed during the audit.
4. No significant deficiencies relating to the audit of the major federal awards programs are reported in the Independent Auditor's Report.
5. The auditor's report on compliance for the audit of the major federal awards programs for Knott County expresses an unqualified opinion.
6. There are no findings relative to the major federal awards programs for Knott County reported in Part C of this schedule.
7. The programs tested as major programs were: U.S. Department of Homeland Security; Disaster Grants - Public Assistance (Presidentially Declared Disasters) (CFDA# 97.036) and U.S. Department of Agriculture; ARRA - Emergency Watershed Protection Program (CFDA# 10.923).
8. The threshold for distinguishing Type A and B programs was \$300,000.
9. Knott County was not determined to be a low-risk auditee.

B. FINDINGS - FINANCIAL STATEMENT AUDIT

FINANCIAL STATEMENT FINDINGS:

2011-01 The Fiscal Court Should Ensure That All Payments Due Are Made Timely

Per an agreement between Perry County and Knott County, Perry County pays 75% and Knott pays 25% of all bonded debt and liability insurance for the Kentucky River Regional Jail. Perry County pays all responsible debt on the Kentucky River Regional Jail, then submits for reimbursement a bill with a copy of the check used to pay that debt with a breakdown of 75%-25% to show the amount owed. For fiscal year ended June 30, 2011, all debt and insurance was paid on behalf of the Kentucky River Regional Jail by Perry County. Upon this payment, Perry County billed Knott County for their share. Knott County did not make this reimbursement of \$53,533 timely. Per KRS 65.140(2) all bills for goods for services shall be paid within thirty (30) working days of the vendor's invoice except when payment is delayed because the purchaser has made a written disapproval of improper invoicing by the vendor. Knott County remitted this payment in November 2012 to cover that balance. Also, during our substantive audit procedures for cash disbursements, we noted several invoices not paid within the thirty (30) day requirement. We recommend that the fiscal court ensure that all amounts owed are paid in a timely manner.

County Judge/Executive Response: Bills are paid when funds are available to pay them.

KNOTT COUNTY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Fiscal Year Ended June 30, 2012
(Continued)

B. FINDINGS - FINANCIAL STATEMENT AUDIT (Continued)

FINANCIAL STATEMENT FINDINGS (Continued)

2012-02 The Fiscal Court Should Ensure That Payroll Timesheets Are Signed And Personnel Folders Are Complete

The test of payroll revealed that timesheets did not always contain proper supervisor signatures or proper employee signatures and that several employee files were missing information for withholdings. Accurate timesheets are required by KRS 337.320 and are necessary to document eligibility for employee benefits, such as retirement. Good internal controls dictate that all employees, except those statutorily exempt from this requirement, maintain and submit timesheets for payroll processing. To further strengthen internal controls, the timesheets should be signed by the employee and by the employee's immediate supervisor for verification and attestation of the accuracy of time reported. Lack of proper internal controls for payroll increases the risk that incorrect payroll information will be processed by the county and that these errors will not be identified and corrected. Also, proper controls will ensure that every withholding from employee's pay is supported in their personnel file with a signed form.

We recommend that the county implement the following internal control procedures to ensure the proper documentation, preparation, calculation and presentation of payroll related items:

1. The county should require all employees to maintain and submit timesheets with daily detail, except those statutorily exempt. Furthermore, the county should require employees and their immediate supervisors to sign all timesheets.
2. The county should ensure that all documentation is in each employee's file for every employee.

County Judge/Executive's Response: Agreed – supervisors should be signing off on timecards. We will take steps to remedy.

2012-03 Knott County Fiscal Court Failed To Fully Restore Restricted Funds

The county's General Fund owed The LGEA Fund \$156,000 at June 30, 2012. During the current year audit, the LGEA Fund made several large transfers to the Road Fund, which were repaid, but the LGEA fund could potentially be in violation of its road expenditure requirements under KRS 42.455.

We recommend the County consult with the Department for Local Government to determine if funds spent by the General Fund and Road Fund would comply with LGEA expenditure restrictions and/or repay the balance.

County Treasurer's Response: All fund transfers between the LGEA and Road funds during my time as treasurer have been repaid. The \$156,000 owed to the LGEA must have been a prior balance. I will make every effort to repay that amount in the future.

KNOTT COUNTY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Fiscal Year Ended June 30, 2012
(Continued)

C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARDS PROGRAM AUDIT

None.

D. SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

None.

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**CERTIFICATION OF COMPLIANCE -
LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAM**

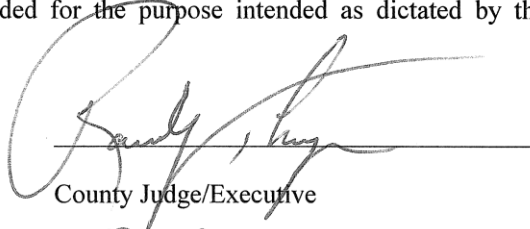
KNOTT COUNTY FISCAL COURT

**For The Fiscal Year Ended
June 30, 2012**

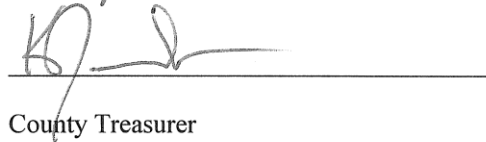
CERTIFICATION OF COMPLIANCE
LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAM
KNOTT COUNTY FISCAL COURT

For The Fiscal Year Ended June 30, 2012

The Knott County Fiscal Court hereby certifies that assistance received from the Local Government Economic Assistance Program was expended for the purpose intended as dictated by the applicable Kentucky Revised Statutes.



County Judge/Executive



County Treasurer

